STATE OF MICHIGAN

SUPREME COURT

CITY OF GROSSE POINTE PARK,
Plaintiff-Appellee,

v.

MICHIGAN MUNICIPAL LIABILITY AND PROPERTY POOL,
Defendant-Appellant.

Supreme Court
No. 125630

Court of Appeals
No. 228347

Wayne County
Circuit Court
No. 98-806998-CK

CITY OF GROSSE POINTE PARK'S BRIEF ON APPEAL

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ORAL ARGUMENT REQUESTED

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STATEMENT OF JURISDICTION

The Pool's statement of the basis of jurisdiction is complete and correct.

STATEMENT OF QUESTIONS PRESENTED

I

WHETHER, IN ORDER TO DETERMINE THE INTENT OF THE PARTIES, THE COURT MAY CONSIDER EVIDENCE OUTSIDE THE FOUR CORNERS OF THE POLICY IN MAKING AN INITIAL DETERMINATION WHETHER THE TERM POLLUTION UNDER THE POLICY IS UNCLEAR AS TO WHETHER IT ENCOMPASSES SEWAGE?

The Court Of Appeals Answered "Yes."

The Trial Court Did Not Answer This Question.

Grosse Point Park Answers "Yes."

The Pool Answers "No."

II

WHETHER THE POOL'S CONSISTENT PRACTICE OF COVERING ALL SEWAGE BACK UP CLAIMS WITHOUT ASSERTING SEWAGE IS POLLUTION CREATES A QUESTION WHETHER THE TERM POLLUTION UNDER THE POLICY ENCOMPASSES SEWAGE?

The Court Of Appeals Answered "Yes."

The Trial Court Did Not Answer This Question.

Grosse Point Park Answers "Yes."

The Pool Answers "No."

III

WHETHER THIS COURT, CONSIDERING THE UNCONTRADICTED EVIDENCE THAT THE POOL COVERED SEWAGE BACK UP CLAIMS UNDER ITS POLICY, CAN DECIDE AS A MATTER OF LAW THAT THE POLLUTION EXCLUSION CLAUSE DOES NOT ENCOMPASS POLLUTION AND THAT THE PARK IS ENTITLED TO JUDGMENT ON ITS COVERAGE CLAIM UNDER COVERAGE A OF THE POLICY?

The Court Of Appeals Remanded This Question For Trial.

The Trial Court Answered "Yes."

Grosse Point Park Answers "Yes."

The Pool Answers "No."

IV

WHETHER UNDER PREVAILING MICHIGAN LAW ON ESTOPPEL, THE PARK HAS DEMONSTRATED SUFFICIENT FACTUAL SUPPORT FOR ITS ESTOPPEL THEORY TO SUBMIT THAT THEORY TO THE TRIER OF FACT FOR DECISION WHERE THE POOL REPRESENTED BY ITS ACTIONS THAT IT COVERED SEWAGE BACK UP CLAIMS AND THE POOL'S TARDY NOTICE OF ITS DECISION TO DENY COVERAGE OUTRIGHT LEFT THE PARK WITH NO REALISTIC OPTION BUT ACCEPT THE TENTATIVE SETTLEMENT IT REACHED AT A TIME WHEN IT THOUGHT IT HAD COVERAGE

The Court Of Appeals Answered "Yes."

The Trial Court Answered "Yes."

Grosse Point Park Answers "Yes."

The Pool Answers "No."

COUNTER STATEMENT OF FACTS

1. **Overview**

This case arises out of Grosse Pointe Park's claim for insurance coverage from the Michigan Municipal Property and Casualty Pool ("Pool") for *Etheridge v. City of Grosse Pointe Park and the City of Detroit,* filed in September, 1995. App. 342a – 368a (*Etheridge* Complaint) Grosse Pointe Park had a series of liability policies from the Pool and asserts that each of the incidents alleged by the *Etheridge* plaintiffs is covered by the policy in effect at the time when the respective incident occurred. Although the Pool admits it has uniformly and consistently paid hundreds of sewage claims for Grosse Pointe Park (the "Park") before, during, and after the *Etheridge* suit and all similar claims asserted by other communities without ever asserting there was no coverage for sewage claims, it denied coverage for the *Etheridge* claim on the ground that sewage is pollution and coverage is barred by the pollution exclusion clause included in the policies.[1]

2. **The Michigan Municipal Property and Casualty Pool**

The Pool is one of several entities established pursuant to MCL 124.5 which permits local governments to establish self-insurance pools. It was organized by the Michigan Municipal League. The Pool describes itself as follows:

> "We provide insurance and risk management services to hundreds of Michigan cities, villages, townships and other governmental agencies. The Michigan Municipal League is our sponsor and administrator. ....Our mission is to be a long-term, stable, cost-effective risk management alternative for members and associated members of the Michigan Municipal League." App. 679b, Michael Forster, quoted at the Pool's web homepage, www.mmlpool.org/public/index.php.

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[1] This case never will repeat itself. The Pool has explicitly halted coverage of sewer backups. App. 685b, Risk Management News, June 2003. The Park has separated storm water from sewage and no longer discharges either to Fox Creek Drain.

The Pool counsel Joel Graziani took pains to clarify for the Circuit Court that the Pool "is not really an insurance company. Rather, it is a pool of municipalities that form together to create procedures to pay for losses. They don't have a ISO forum, they do the best they can to try to help their members." App. 237a-238a.

3. **The Insurance Policies**

From August, 1985 through July, 1998 Grosse Pointe Park obtained a series of 13 successive insurance contracts with the Pool with coverage beginning on August 1 under each policy. Each policy period ran from August, 1 to July, 30 of the following year. All of the policies are substantially the same. App. 508b – 568b, 1994/1995 Policy ("Policy"). Because the policies are "occurrence" and not "claims made" policies, the claim for the July 24, 1995 event falls under the policy in effect from August 1, 1994 to July 30, 1995, when the alleged flooding occurred, and not under the August 1, 1995 to July 30, 1996 policy, the policy which was in effect when the claim was received. The *Etheridge* complaint alleges other flooding events which fall within the appropriate policy years according to the same logic.

Under the Policy, the Pool provided several coverages triggered by the allegations in the *Etheridge* complaint including Coverage A - Bodily Injury and Property Damage Liability; and Coverage D - Public Officials Errors & Omissions. App. 514b, 521b, Policy, §I - Municipal Liability Coverage. The Court of Appeals affirmed the trial court's determination that the *Etheridge* claims fell within Coverages A and D. The Court of Appeals' decision that coverage is provided under Coverage A for the Park's alleged liability to the *Etheridge* plaintiffs will remain undisturbed unless the "pollution exclusion" clause applies to defeat the Park's claim.

The pollution exclusion clause appears at Section V.d. of the Policy. App. 326a-328a. It excludes coverage for Bodily Injury or Property Damage arising out of the actual release, discharge or escape of pollutants. App. 327a. Pollutants are defined as

> "[A] any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste. Waste includes materials to be recycled, reconditioned or reclaimed." App. 328a.

The definition does not expressly mention sewage, sewer flow, storm water flow or combined sewage flow. The Pool does not have any documents or manuals which interpret or construe its pollution exclusion clause. App. 8b, Defendant's Responses to Plaintiff's First Discovery Requests, response to Request 12.

4. **History of Fox Creek Drain**

The Fox Creek Drain received sewage flow for many years from Detroit and the Park. But, in the period during which the Pool insured the Park, discharges were made pursuant to a state environmental permit which permitted such discharges whenever rain or storm flows threatened to overwhelm the Park's sewer system and cause sewage back ups in the Park. Judge Hathaway, who was intensely involved in the *Etheridge* case and had appointed a special master to advise her on alternatives to the diversions of excess flow to the Fox Creek Drain, repeated throughout the hearing on the parties' summary disposition motions that the Pool's suggestions that the Park had any kind of intent or willingness to harm the properties in Detroit with its discharges to the Fox Creek Drain were utter nonsense:

> "To ever [sic] suggest time and time again that the intent was to ruin homes in Grosse Pointe and/or to ruin homes on Fox Creek is beyond this Court's conception. The Court is more than satisfied that the intent was not to cause harm. The intent was to avoid harm." App. 206a – 268a, January 7, 2000 Hearing Transcript p 6. See also Transcript at pp 8, 11, and 19-20.

Since 1995, the Park has separated its sewer system and has permanently blocked the discharge point to Fox Creek Drain.

5. **The *Etheridge* Suit**

On September 14, 1995, Doris Etheridge filed a putative class acting on behalf of herself and others alleging their homes were flooded by Grosse Pointe Park's discharge of sewage into

Fox Creek Drain on July 24, 1995 and other dates. App. 324a – 368a, *Etheridge* Complaint. The *Etheridge* plaintiffs alleged the combined sewer flow into the Fox Creek Drain interfered with the use and enjoyment of their property as a result of "the flooding and physical invasion of Plaintiffs' property by dirt, debris, ... water, and untreated sewage, thereby causing material injury to Plaintiffs' person and property through trespass, gross negligence, ... and nuisance." App. 409a – 416a, *Etheridge* Second Amended Complaint, ¶ 2. The "discharge into Fox Creek overflows the boundaries of Fox Creek onto the property of Plaintiffs." *Id* at ¶ 22. "The volume of the Defendants' discharge caused the sewers servicing Plaintiffs' residences to back up into Plaintiffs' basements." *Id* at ¶ 43

6. **The Pool Has Had a Consistent and Uniform Practice of Covering Sewage Claims And Not Invoking the Pollution Exclusion**

The Pool has covered several hundred claims from Grosse Pointe Park for sewage releases, App. 1661a – 1716a, Account Loss History, as shown below. The Pool covered 3 claims under the 1994/1995 policy before it denied the *Etheridge* claim.

HISTORY OF COVERAGE FOR SEWAGE CLAIMS			
Policy Year	**Date of Loss**	**No. of Claims**	**Coverage Position**
1992/1993	August 18, 1992	1	Covered
1993/1994	July 6, 1994	68	Covered
1994/1995	March 7, 1995	1	Covered
1994/1995	July 6, 1995	1	Covered
1994/1995	July 13, 1995	1	Covered
1994/1995	July 24, 1995	*Etheridge* (Approximately 300 claimants)	Denied
1995/1996	June 18, 1996	*Walters,* (207 claims)	Covered
1997/1998	September 7, 1997	1	Covered

All of these claims were handled by the Pool without a reservation of rights or denial of coverage with regard to the pollution exclusion clauses, except for the claims made in the

Etheridge case. App. 711b-713b, Tucker Dep, pp 155-156. Any claims that were denied were not denied on the basis of the pollution exclusion. *Id.* The claims were settled on an ongoing basis between January, 1994 and 2000. Thus, sewage-related claims were received and settled before, during and after the period of the *Etheridg*e suit (September, 1995 to September, 1997).

Several covered claims involved widespread sewage backups in Grosse Pointe Park in July, 1994 and June, 1996 which resulted from intense rainstorms. The July, 1994 sewage backup resulted in 68 claims in 1994. The Pool's investigation in the summer of 1994 revealed that Grosse Pointe Park had a combined sewer system which carried both sanitary and storm flow and that if the system of the pump station cold not handle the flow, sewage would back up into basements. See App. 641b – 670b. No reservation of rights letter was issued and the claims were covered without any objection by the Pool.

The June, 1996 release resulted in a class action lawsuit, *Walters v Grosse Pointe Park,* Wayne Co Cir Ct Case No. 96-647109, filed on November 19, 1996. App. 1614a – 1635a. The *Walters* complaint alleged that "untreated sewage backed-up into plaintiff homeowners' basements," Complaint, ¶ 1, and that

> "'Sewage' means urine, feces, blood, other human bodily fluids, toxins, bacteria including e. coli, microbes, viruses, including hepatitis, HIV and AIDs viruses, ... chemicals, fertilizers, other elements of sewage, combined sewage overflow, ...rainwater, debris, ... sewer influent of every kind and nature ... and components of sewage which may have been contained in the solutions which backed up or came into the homes of the Plaintiffs. Sewage includes these solutions, whether fully treated, partially treated, or untreated." App.1615a, *Walters* Complaint, ¶ 2.

On December 18, 1996, the Pool issued a coverage letter stating "In review of the Summons and Complaint, coverage is being afforded ... through your coverage with the ... Pool." App. 626b, *Walters* First Reservation of Rights Letter. The *Walters* plaintiffs later filed an amended complaint, seeking injunctive relief in addition to damages. On April 21, 1997, the Pool issued a reservation of rights letter as to the injunctive relief sought in the amended

complaint but still did not invoke the pollution exclusion clause. App. 1636a – 1637a, *Walters'* Amended Reservation of Rights letter. Those claims were all settled by a class action settlement in 2000 funded by the Pool.

The Pool admits that it has for years paid property damage claims resulting from discharge of sewage without invoking the pollution exclusion clause. *See,* Pool S Ct Brief at 10.

As of December, 1999, the Pool's claim manager testified that Pool had never invoked the pollution exclusion to deny coverage for *any* sewage damage claims received from *any* of the Pool's participating communities[2]. App. 711b-713b, Tucker Dep, pp 56-57. That was a very large number of claims indeed: "[S]ince January 1, 1990, the Pool has opened 2,707 sewer case files involving thousands of events or occurrences." App. 18b, Pool's Brief in Support of Defendant's Answer To Plaintiff's Motion To Compel Answers To First Discovery Request, p 8 (February 3, 1999).

The Pool conceded during argument on the summary disposition motions that that there was no difference between the sewage discharged into Grosse Pointe Park residents' basements and covered by the Pool and the discharges into Fox Creek:

> "With the substance itself, Your Honor, there isn't any difference. But that doesn't give you any information under the law by which to interpret the application of the pollution exclusion in this case for the reasons that I've stated." App. 232a, Hearing Transcript, p 27, Argument of Joel Grazianai, the Pool's attorney.

It is a matter of general knowledge that municipal insurers in Michigan did write policies which covered basement backups. The Detroit News, in an in-depth article on basement flooding from sewer back ups and the then-pending *Pohutski* case, reported in early 2002 that the

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[2] The Park sought detailed discovery from the Pool with regard to how it handled other sewage claims but the trial court barred that discovery. The trial court's discovery order was

Pool and the Michigan Municipal Risk Management Authority ("MMRMA") had provided coverage for basement backup claims since in the 1980s. App. 680b – 683b, *Cities worry coffers will run dry in flood lawsuits*, Detroit News, January 10, 2002, www.detnews.com/2002 /metro/0201/11/a01-387141.htm.

The Pool publicly acknowledges that it covered sewer backups until April 2000 when basement flooding claims had finally mounted to a point too expensive to insure. In the above Detroit News article, Mike Forster, claims manager for the Pool, was quoted as saying that "the recent explosion of class-action lawsuits filed against Michigan cities has forced his agency to drop most of its flood coverage in southeast Michigan." In a March 2002 report to its members, available on the Web, the Pool explained that the reason for an increase in open lawsuits in 2001 "is that a large number of sewer backup claims from previous years are still open, awaiting the Michigan Supreme Court's ruling on *Pohutski v. Allen Park* before settlement discussions proceed." App. 689b – 690b, *Pool claims continue downward trend*, MML Risk Management News, March 2002, www.mmlpool.org/shared/public/publications/newsletter/march02/ index.php. A year later, Kevin Murphy, the Pool's administrator, reported that its financial status had strengthened. "He said that it has taken three years since the decision to exclude sewer back-up coverage in April, 2000 ... for the Pool's financial position to improve." App. 685b – 686b, *Pool surplus rebounds! Can rate stability be far behind?* MML Risk Management News, June 2003, www.mmlpool/shared/public/publications, newsletter/june03/index.php.

This Court has recognized that insurance was generally available in the 1990s to municipalities for sewer back ups. *Pohutski v Allen Park,* 465 Mich 675; 641 NW2d 219, (2002), arose out of a sewer back up event in February 1998. This Court gave its decision

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appealed to the Court of Appeals which did not address the issue. App. 316b – 376b,

prospective application because municipalities had relied on insurance to cover liability risks of what was understood to be trespass/nuisance exceptions to governmental immunity.

> "Second, there has been extensive reliance on *Hadfield*'s interpretation of § 7 of the governmental tort liability act. In addition to reliance by the courts, insurance decisions have undoubtedly been predicated upon this Court's longstanding interpretation of § 7 under *Hadfield*: municipalities have been encouraged to purchase insurance, while homeowners have been discouraged from doing the same. Prospective application acknowledges that reliance." *Pohutski,* 465 Mich at 697.

As this Court correctly recognized in *Pohutski*, Allen Park was insured for sewage back ups. The Pool was its insurer and covered the settlement which was reached very shortly after the *Pohutski* decision. *See*, App. 395b, the Pool's settlement check for $1,200,000.

7. **Grosse Pointe Park Has Provided Evidence Which Support Application Of Estoppel.**

The factual record of the Pool's actions during the Etheridge case is extensive and demonstrates a pattern of settling basement back up claims with full knowledge that the substance in the basements was sewage. The detailed chronology is set forth in the Appendix at App. 714b-717b. It is clear that from July, 1994, the Pool understood that the liquid involved in these backups contained sewage.

In addition to the Pool's practice of covering all other sewage claims made by the Park, it participated in the *Etheridge* settlement negotiations in a way which lead the Park to believe, at the time it reached a settlement in the case, that the *Etheridge* claim was covered. Between 1995 and August 1997, the Pool participated actively in oversight of the *Etheridge* case, received all pleadings, and attended conferences with the court. App. 704b-710b (Garrison dep, p 315-316).

In June, 1997, the trial court set a September trial date and ordered the parties into facilitation before former Judge Richard Kaufman. App. 905a – 911a. On July 24, 1997, the

Pool meet with Grosse Pointe Park to discuss settlement in *Etheridge*. Meadowbrook and Pool representatives agreed to recommend at least $750,000 authority for the Park. Defense counsel, John McSorley, advised that settlement would probably require much more than $750,000. App. 697b-703b (Forster dep, p 48), App. 704b-710b (Garrison dep, pp 189-192). On July 28, 1997, Mr. McSorley met with Pool and advised of the likelihood of an adverse verdict and damages that might approach $20 million. App. 1645a – 1655a. Immediately thereafter, the Pool asked its outside counsel for a coverage opinion.

On or about August 4, 1997, on advice of outside counsel, the Pool decided to deny coverage of the *Etheridge* claims. App. 697b-703b (Forster dep, pp 84-86). The Pool directed Pamela Garrison, the claims agent working with Grosse Pointe Park, that "everyone" be notified immediately, but no written or other notice was sent to the Park. *Id.* No one told the Park before the first facilitation session. On August 10, 1997 Ms. Garrison actively participated in the first facilitation meeting and did not mention the denial of coverage then. After the facilitation meeting, Ms. Garrison mentioned to City Manager Krajniak only that there were "potential coverage issues" but did not say coverage was denied. App. 912a – 914a, Garrison Status Report, August 11, 1997. Garrison testified that she was aware that the final decision to deny coverage had been made prior to the second facilitation, yet she did not convey that to the Park. Instead, she continued to participate in the facilitation process. App. 97b-103b (Garrison dep, pp 229, 231, 235, 238-240, 242, 243, 246, 254-257.) On August 11, Ms. Garrison sent Grosse Pointe Park a letter requesting a meeting. The letter did not even reference coverage, much less state that the decision to deny coverage had been made the week before. App. 915a. This was contrary to the Pool's Claims Operations Manual which states that the insured will be sent a "denial letter" when coverage is denied. App. 691b-692b, Meadowbrook Claims Operations

Manual, Section 3.10. Also on August 11, 1997, Mr. McSorley wrote Meadowbrook to obtain $2.5 million settlement authority. App. 1657a – 1660a. Although two weeks elapsed before the next facilitation, the Pool did not reply in that interval and inform Mr. McSorley that it was not covering the claim.

On Sunday, August 26, 1997, Judge Kaufman convened the second facilitation meeting and the parties settled the case for $3.8 million with Grosse Pointe Park and Detroit, App. 100b, (Garrison dep, pp 242-243) splitting the settlement equally. Ms. Garrison participated in the negotiations and approved the settlement.

On August 27, 1997, the Pool finally told Grosse Pointe Park it was denying all coverage. App. 472a. On September 3, 1997, the Pool sent a letter to the Grosse Pointe Park explaining its decision and inviting a response. App. 635b – 640b. On September 4, 1997, notwithstanding its letter of September 3 to the Park, the Pool advised its Board that the Park's insurance claim had been denied. App. 697b-703b (Forster dep, pp 103-104). Board action is only required if coverage is recommended in an amount greater than $100,000.

The Park went ahead with the settlement, notwithstanding the Pool's refusal to cover. The Park felt it had little choice but to accept the settlement after considering "the potential liability and the potential adverse consequences were we to reject the settlement on the basis of no liability coverage." App. 556a (Deason dep, p121-122).

SUMMARY OF ARGUMENT

Although all can agree that sewage flow is repugnant, unhealthy and is commonly regarded as pollution by the government and the man in the street, there is nothing to prevent two parties from entering into a contract to insure against claims arising from sewage backups. This appeal addresses whether, notwithstanding its undesirable qualities, the Pool chose to insure its Member municipalities, which handle sewage by the billions of gallons, against tort claims arising out of releases of that sewage from the municipality's sewer system onto private property. There is nothing far fetched about such a proposition. To the contrary, it would seem to be the kind of municipal risk that a local government self insurance pool would choose to cover. All evidence supports the conclusion that the Pool did write such coverage; it admits it settled literally thousand of sewer back up claims without once claiming that sewage was pollution within the meaning of the pollution exclusion clause in its policy.

At the center of this case is the pollution exclusion clause and its definition of pollution. The clause bars coverage for damages caused by pollution. The express definition of pollution in the contract is generic in form and does not expressly mention sewage. The Pool says in this case that the term pollution should be interpreted to cover sewage and that that is the only interpretation possible of that term under its contract -- notwithstanding that it has covered every other sewage claim without asserting sewage was pollution. But, it offers no explanation why all of the other sewage back ups were not pollution too.

Instead the Pool tells this Court that it must ignore the admitted truth that it covered thousands of other sewage backup claims asserted against the Park and other communities. Like the tailor in "The Emperor's New Clothes" and the little man behind the curtain in the Wizard of Oz, the Pool asks this Court to proceed as if something obviously true were not. As explained

below, that is not Michigan contract law. Such a rule will defeat the very contract principle the Pool claims to protect – the right of parties to have the court enforce the agreement they made.

This case is grounded on the uniformly accepted premise that the court's role in a contract dispute is to determine the intent of the parties and to enforce it. Courts have long recognized that a wide variety of evidentiary materials can inform the court with regard to the parties' actual intent. The courts and commentators agree that a party's course of performance during the contract is highly probative of that party's construction of the contract.

This Court has asked whether extrinsic evidence can be used to determine whether a disputed term in a contract is capable of only one meaning, that is, whether the contract is ambiguous. Again, the answer in Michigan and elsewhere is "Yes."

It is the general rule that a court will consider, as a preliminary matter, extrinsic evidence to determine whether a contract has a latent ambiguity, where language "suggests but a single meaning, but some extrinsic fact or extraneous evidence creates a necessity for interpretation or a choice among two or more possible meanings...." Black's Law Dict (5th ed), p73. The courts, including this Court on numerous occasions, and the commentators have long recognized that contracts apparently clear on their face may not be. They have acknowledged the trial court's role in making an initial determination whether there is a real material factual dispute as to whether a contract's meaning is as really clear as a reading, uninformed by the circumstances, would indicate.

The Pool urges this Court to adopt a new rule of law that would bar trial courts from considering any evidence with regard to the meaning of the terms of a contract if the court

determines, without considering any evidence other than the language of the contract itself, that the meaning of the language is clear and not capable of more than one meaning.[3]

The policy reasons offered by the Pool for adoption of this rule are flimsy – the Pool relies on the rubrics of "freedom of contract" and "questions of contractual ambiguity are questions of law for the court," and on repeated references to the parol evidence rule and cases involving that rule.

The Parol Evidence Rule, which bars the court from considering any evidence of prior or contemporaneous agreements in order to add, delete or contradict terms of a written contract which a court has determined to be a complete expression of the parties' agreement, has no application here. The Parol Evidence Rule does not apply to evidence offered to assist the courts in determining the meaning of a contractual term which the parties agree is part of the contract. The Pool and the Park agree that their contract has a pollution exclusion clause and an express definition of the word pollution. Because that express definition does not specifically mention sewage and because the Pool has covered thousands of other sewage claims, the parties disagree whether the term pollution in the pollution exclusion clause encompasses sewage.

As to the "question of law" argument, that phrase is a fiction for the fact that courts have long determined that factual questions in some circumstances will reserved to the judge and not given to the jury. The question whether the meaning of a term in a contract is capable of more than one meaning in the context of the contract is one which courts have long reserved to themselves. The Park does not argue it should be otherwise. What the Pool advocates is a rule

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3 Such a rule is appropriately described as naïve. Even under such a rule, it must be recognized that the court will still bring extrinsic material outside the contract to bear in making that decision – that extrinsic material being the judge's own unique knowledge and experience. Corbin, *The Interpretation of Words and the Parol Evidence Rule*, 50 Cornell Law Quarterly 161, p 164 (1965).

preventing a court from making that factual determination by preventing the court from considering any evidence beyond the contract. That rule will pervert the court's role in interpreting contracts. It will prevent a court from enforcing the contract the parties have made because in many instances it will prevent the court from discovering just what that contract was. It will substitute a judge's opinion whether a term is susceptible to only one meaning for that of the parties. Thus the proposed rule runs counter to freedom of contract which is premised on the parties' constitutional right to have the court enforce the agreement they made.

In this case, when the court looks to extrinsic evidence to see whether the term pollution in the contract may not encompass sewage, it will find the best kind of evidence, the Pool's consistent actions under the subject contract and other similar contracts. Courts recognize that the best evidence of a party's interpretation of a contract is its prior performance of the contract. Here, the Pool paid every other sewage claim under its contracts with the Park, literally hundreds of individual claims before, during and after the *Etheridge* case, without asserting that sewage was pollution. Further, it admits that in the same period it paid on literally thousands of claims by other municipalities which it insured. There is a second form of compelling evidence. The Pool admits in public statements on its website on the Worldwide Web and in a newspaper article that it covered sewage backups until April 2000. Thus at the least, that extrinsic evidence raises a question whether pollution *in this contract* includes sewage. In fact, because that evidence is uncontradicted and the Pool has offered no evidence to differentiate the sewage in *Etheridge* from the sewage in all of the other claims, the Court should determine as a question of law that pollution does not encompass sewage and enter judgment in the Park's favor.

The estoppel issue accepted by this Court on appeal addresses the question whether the Park has plead an action for estoppel within the permitted exceptions in insurance law and

whether at a minimum the Park provided the trial court with sufficient evidence to resist a summary disposition motion. The Pool appeals the trial court's and the Court of Appeal's denial of its "(C)(10)" motion to dismiss the Park's claim that the Pool is estopped from raising the pollution exclusion defense to coverage. The Pool acknowledges that there are limited circumstances in which an insurer may be estopped from denying coverage. It argues that the Park has not proved those circumstances. The posture of this case is such that the Park need not "prove" anything at this time –it will resist summary disposition if it provides some evidence which creates a question of fact on the elements of the estoppel claim. In evaluating what the Park has brought forward, the court is required to construe all inferences and all evidence in the Park's favor. It is clear that Judge Amy Hathaway, who as presiding judge was intimately familiar with the facts of the underlying *Etheridge* lawsuit, concluded that the Park so convincingly proved those circumstances and the Pool's failure to rebut was so complete that judgment could be granted in the Park's favor. The Court of Appeals agreed that the Park had demonstrated sufficient factual support for estoppel but found the demonstration was not so one-sided as to permit summary disposition in the Park's favor. Appellate courts rightly extend substantial deference to a trial court's evaluation of factual matters. This Court need only agree that there is a genuine question of material fact as to each of the elements of estoppel to decide this appeal on this issue in the Park's favor.

ARGUMENT

The Supreme Court has certified three issues on appeal:

- Is sewage encompassed within the definition of "pollution" under the contract between the Park and the Pool?
- Can we look to extrinsic evidence to determine whether the meaning of pollution vis a vis sewage under the contract is capable of more than one meaning?
- May the Park proceed on an estoppel theory to prevent the Pool from denying coverage in this case, even if sewage is encompassed within the term pollution?

We believe the proper order of the questions begins with whether a court in construing a contract between the parties may consider all of the facts and circumstances surrounding the contract and its performance in determining whether a relevant contract term is capable of more than one meaning? The answer to this question determines how we may go about answering whether sewage is encompassed within the term "pollution" in the contract between the Park and the Pool.

I

STANDARD OF REVIEW

The case comes to this Court on appeal from summary disposition motions granted and denied pursuant to MCR 2.116(C)((10). A decision by a trial court on a motion for summary disposition is subject to *de novo* review. *Hazle v Ford Motor Co*, 464 Mich 456, 461; 628 NW2d 515 (2001); *Sprague v Farmers Ins Exch*, 251 Mich App 260, 264; 650 NW2d 374 (2002). A summary disposition motion under (C)(10) is properly granted where there is no genuine issue of material fact, entitling the moving party to judgment as a matter of law. *Hazle, supra*; *Sprague, supra*. In deciding a (C)(10) motion, all evidence must be reviewed in the light most favorable to the non-moving party, *Hazle, supra,* and all reasonable factual inferences must be drawn in favor of the non-moving party. *Jackson v City of Detroit*, 449 Mich 420, 426; 537 NW2d 151 (1995). The opposing party may not rest on its denials but must provide evidentiary material to

raise legitimate questions of material fact. *Sprague* at 264. Summary disposition under (C)(10) is property granted if the non-moving party fails to do so. *Id.*

II

IT IS A WELL ESTABLISHED RULE THAT A COURT SHOULD CONSIDER EVIDENCE OUTSIDE OF THE "FOUR CORNERS" OF A CONTRACT IN ORDER TO DETERMINE WHETHER RELEVANT PROVISIONS OF THE CONTRACT ARE SUSCEPTIBLE OF MORE THAN ONE MEANING.

(a) The Court Is Obliged To Consider Evidence Of A Contract's Meaning So That It Can Enforce The Contract The Parties Made.

> "The general rule [of contracts] is that competent persons shall have the utmost liberty of contracting and that their agreements voluntarily and fairly made shall be held valid and enforced in the courts. Under this legal principle, the parties are generally free to agree to whatever they like, and, in most circumstances, it is beyond the authority of the courts to interfere with the parties' agreement. Respect for the freedom to contract entails that we enforce only those obligations actually assented to by the parties." *Wilkie v Auto-Owners Ins Co*, 469 Mich 41, 62-63; 664 NW2d 776 (2003) (internal cites omitted).

The accepted process for resolving questions involving the disputed meaning of contract terms is well summarized as follows:

> "Although the meaning of language is really a question of fact, in many instances it has been determined that this question should be treated as a question of law in the sense that the determination should be made by the trial judge. The general rule is that the interpretation of a writing is for the court. Where, however, the meaning of a writing is uncertain or ambiguous and extrinsic evidence is introduced in aid of its interpretation, the question of its meaning should be left to the jury except where, after taking the extrinsic evidence into account, the meaning is so clear that reasonable men could reach only one conclusion, in which event the court should decide the issue as it does when the resolution of any question of fact is equally clear." Calamari & Perillo, *A Plea For a Uniform Parol Evidence Rule and Principles of Contract Interpretation*, 42 Ind LJ 333, 351 (1967); *citing* 3 Corbin on Contracts[4] (1960) § 538, and 4 Williston, § 616[5].

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[4] This Court's citations with approval to Corbin are too numerous to list. Most recently in *Wilkie v Auto-Owners Ins Co*, 469 Mich 41, 52; 664 NW2d 776 (2003), the Court described Corbin on Contracts as a "definitive study of contact law."

[5] This section is now § 30.7 in the latest edition, 11 Williston on Contracts (4th ed).

Of course, one cannot determine whether a writing is certain or unambiguous without knowing the surrounding circumstances, 3 Corbin on Contracts (1960) § 542, requiring the consideration of extrinsic evidence if an issue of ambiguity is raised. In coming down on the side of using extrinsic evidence to determine ambiguity and the intent of parties, Corbin advises that:

> "The less one knows about the history and evolution of language, the more likely he is to suppose that he knows the 'true meaning' of words, and the more likely he is to hold that the words used by the contracting parties have a 'legal meaning' or a 'plain and clear' meaning. This leads to decisions that testimony, however, plausible, showing what the words actually meant to one or both of the contracting parties, is excluded by the 'parol evidence rule.'" 3 Corbin on Contracts (1960), § 579, p 428.

This Court's observations in *Davis v Kramer Bros Freight Lines, Inc*, 361 Mich 371, 375; 105 NW2d 29 (1960), are instructive.

> "The trial court took the position that plaintiffs were 'trying to change the terms of the contract.' But before we can recognize a change in the terms of a contract we have to determine what the terms are. The initial issue on the contract is a matter of the interpretation of the words used. We know that a word, to use Mr. Justice Holmes' expression, is 'flexible.' Its meaning must be ascertained in the light of all of the relevant circumstances, not excluding, where helpful, 'the experience of courts and linguists,' *and including, as well, the meanings accepted by the parties.* * * * Today words themselves are not so powerful, for we are well aware that words are not 'transparent and unchanged,' but 'may vary greatly in color and content according to the circumstances and the time in which [they are] used.'" Footnotes and citations omitted, emphasis added.

Michigan courts have long recognized the need to examine all of the circumstances surrounding a contract when called to interpret its terms. *Davis v Belford*, 70 Mich 120, 126; 37 NW2d 919 (1888):

> "In the construction of contracts, the court will look at all the circumstances of the case, the nature of the property, the residence, occupations, and relations of the parties, the usages of the place, and of the business to which the contract relates, and ascertain, by reasonable inference, what the parties must have understood and mutually expected at the time of the making of the contract, and then adopt that construction which will best and most nearly carry the contract into effect as they intended and understood it." Citation omitted.

To like effect, 2 Restatement Contracts, 2d, § 212(1), Interpretation of an Integrated Agreement. Comment b to § 212, p 126, explains,

> "The rule stated in Subsection (1) is not limited to cases where it is determined that the language used is ambiguous. Any determination of meaning or ambiguity should only be made in the light of the relevant evidence of the situation and relations of the parties, the subject matter of the transaction, preliminary negotiations and statements made therein, usages of trade, and the course of dealing between the parties."

(b) Michigan Courts Have Always Considered Evidence Outside Of The "Four Corners" Of A Contract To Determine If A Disputed Term Is Ambiguous.

A latent ambiguity exists "where the language employed is clear and intelligible and suggests but a single meaning, but some extrinsic fact or extraneous evidence creates a necessity for interpretation or a choice among 2 or more possible meanings." *McCarty v Mercury Metalcraft Co*, 372 Mich 567, 575; 127 NW2d 340 (1964), *cert den*, 380 US 952; 85 SCt 1085; 13 Led 2d 969 (1965). In *McCarty*, a unanimous court pointed out that "[s]ince the detection of latent ambiguity requires a consideration of factors outside the instrument itself, extrinsic evidence is obviously admissible to prove the existence of the ambiguity, as well as to resolve any ambiguity proven to exist." *Id.* In *Goodwin, Inc v Orson E Coe Pontiac, Inc*, 392 Mich 195, 206; 220 NW2d 664 (1974), a unanimous court held that:

> "[McCarty] is significant for our inquiry in two respects. First, it recognizes that the detection of an ambiguity requires admissibility of extrinsic evidence to prove it or, as in this case, disprove it, 'as well as to resolve any ambiguity proven to exist.' Second 'extrinsic evidence is admissible to *indicate the actual intent of the parties*.'" (emphasis in original).

After discussing *McCarty* and other cases, the *Goodwin* court held, 392 Mich at 209-210:

> "From these cases we derive the following rules to decide this case:
>
> "1) Where ambiguity may exist in a contract, extrinsic evidence is admissible to prove the existence of ambiguity.
>
> "2) Where ambiguity may exist in a contract, extrinsic evidence is admissible to indicate the actual intent of the parties.

> "3) Where ambiguity exists in a contract, extrinsic evidence is admissible to indicate the actual intent of the parties as an aid in the construction of the contract."

Other Michigan courts have repeatedly and consistently held that extrinsic evidence may be used to show or resolve a latent ambiguity. In *Keller v Paulos Land Co*, 381 Mich 355, 360-362; 161 NW2d 569 (1968), the court approved that admission of testimony and a survey to demonstrate that term "nonexclusive easement of ingress and egress" actually was not intended to permit access or egress over the burdened property but was intended solely to permit parking; *By-Pas Intl Corp v By-Pas Mfg Corp*, 431 Mich 896; 431 NW2d 823 (1988) (peremptorily reversing Court of Appeals decision, citing *Goodwin*, and reinstating holding of the circuit court where "Evidence establishing and explaining the [latent] ambiguity was properly admitted without objection by the trial court and was properly used in resolving the ambiguity."); *Hall v Equitable Life Assurance Soc*, 295 Mich 404, 408; 295 NW 204, 206 (1940) ("It is a well-settled rule that extrinsic evidence is permissible to show that a latent ambiguity exists.").

See also, 2 Restatement Contracts, 2d, §214(c). "Even though words seem on their face to have only a single possible meaning, other meanings often appear when the circumstances are disclosed." *Id* at Comment b, p 133.

This Court has adopted the same rule for the construction of wills and trusts. *In re Estate of Kremlick*, 417 Mich 237, 240-241; 331 NW2d 228 (1983).

> "Determining the presence of a latent ambiguity, however, is more difficult. This Court has held that in interpreting contracts where an ambiguity *may exist*, extrinsic evidence is admissible: (1) to prove the existence of ambiguity; (2) to indicate the actual intent of the parties; and (3) to indicate the actual intent of the parties as an aid in construction.... These rules are equally applicable to interpreting wills. Thus, not only may extrinsic evidence be used to clarify the meaning of a latent ambiguity, but it may be used to demonstrate that an ambiguity exists in the first place and to establish intent."

See also, *In re Estate of Traub*, 354 Mich 263, 280; 92 NW2d 480 (1958), citing with approval, 3 Corbin on Contracts (1960), § 579, pp 420-21, "'As long as the court is aware that there may be doubt and ambiguity and uncertainty in the meaning and application of agreed language, it will welcome testimony as to antecedent agreements, communications, and other factors that may help to decide the issue.'" *Oades v Marsh*, 111 Mich 168; 69 NW 251 (1896), (extrinsic evidence considered to determine that testator's bequest of one share of stock actually referred to twenty shares of stock.)

As the dissent noted in *Beason v. Beason* (after remand), 204 Mich App 178, 185-186; 514 NW 2d 231 (1994) , *peremptorily rev'd*, 477 Mich 1023, 527 NW2d 425 (1994), "Ordinary English words can be deprived of their ordinary meanings and supplied with others – even with meanings that are the exact opposite of their ordinary ones," citing 3 Corbin on Contracts (1960), § 544, p 155. In *Beason*, the question was whether the term providing that alimony would terminate "'when [defendant] should reside with an unrelated adult male person'" was ambiguous. After one trip up to the Supreme Court and back to the trial court, the trial court concluded that the term "reside" was ambiguous but resolved its meaning by looking to Black's Law dictionary and did not reopen proofs to take evidence on what the parties might have meant by the term "reside" in their divorce decree. The Court of Appeals disagreed and concluded that the term was not ambiguous. The dissent observed however, "When the [Supreme] Court instructed the trial court to consider 'the meaning of the term "reside" in the parties' divorce judgment,' must this not have meant that its meaning in the judgment could be different than its meaning in other judgments?" *Beason*, 183. The dissent concluded that "If the evidence adduced caused the trial court to conclude that the parties agreed with regard to the meaning of the work 'reside,' then that is the meaning that should have been applied to the already existing

record concerning the conduct of the [parties]." *Id* at 186. Clearly, the Supreme Court's subsequent reversal in *Beason* is a strong sign it agreed with the dissent's reading.

The decisions show that words and phrases with apparently clear or obvious meanings to the court had other meanings to the parties. In *Beason*, the disputed phrase was "reside with an unrelated male person." That is not apparently ambiguous but, although we all think we know what "reside" means and who a "male person" is, this Court concluded that the trial court should take evidence from the parties to determine what *they* intended. The easement for "access and egress" in *Keller* seems clear enough, yet the court determined it did not mean access or egress at all but parking instead. The bequest of one share of stock in a corporation in *Oades* seemed clear on its face, yet it turned out, when the testator's circumstances were taken into account, he was actually referring to twenty shares, not one. In each case, after considering evidence outside the contract the courts concluded the terms meant something different than might appear at first glance.

The dissent's reasoning in *Beason* applies here. Just as a divorcing couple may enter into a stipulated judgment using terms with meanings special to that agreement, the Park and Pool entered into an insurance contract where terms used had meanings different than those in many other policies of insurance between other parties. Where the express definition of pollution in the Pools' policy does not specifically use the term sewage, the court should appropriately inquire whether the parties intended it to include sewage when extrinsic evidence (all of it adduced from the Pool itself) shows that its policy uniformly covered sewage backup claims asserted by members of the Pool including the Park until early in 2000.

(c) The Rule That Extrinsic Evidence May Be Used To Show The Existence Of A Latent Ambiguity Is Widely Recognized By Courts In Other Jurisdictions.

Typical of other decisions in the court's holding in *Lincoln Elec Co v St. Paul Fire & Marine Ins. Co*, 210 F3d 672, 683-685, n 12 (6th Cir, 2000) (Ohio law):

> "Extrinsic evidence can become a consideration *before* an ambiguity has been identified from the face of the contract as a matter of law, in the limited sense that such evidence can assist the court in determining whether, as a matter of law, two plausible interpretations exist in the manner necessary to give rise to the existence of an ambiguity....Obviously, the natural and ordinarily meaning of language, reasonable construction of a contract, surrounding circumstances, and positions and actions of the parties are issues that cannot be weighed in a vacuum. ... Thus, the district court may take cognizance of extrinsic evidence in order to determine whether a factfinder need consider parol evidence in construing the contract." Emphasis in the original.

Like holdings are numerous.[6]

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[6] See also *Interstate Investment Corp v Rose Care, Inc*, 631 So 2d 836, 839 (Ala 1993) ("If the language of a contract...contains a latent ambiguity, extrinsic evidence, including evidence of the surrounding circumstances and the construction placed on the language by the contracting parties, may be considered in determining the meaning of a contract.."); *Hamada v Valley National Bank*, 27 Ariz App 433; 555 P2d 1121 (Ariz App Div 1 1976) ("Since the detection of a latent ambiguity requires a consideration of facts outside the instrument itself, extrinsic evidence is obviously admissible to prove the existence of the ambiguity, as well as to resolve any ambiguity proven to exist."); *Wolf v Superior Court of Los Angeles County*, 114 Cal App 4th 1343, 1351; 8 Cal Rptr 3d 849, 655-656 (Cal App 2d Dist 2004) ("a latent ambiguity may be exposed by extrinsic evidence which reveals more than one possible meaning to which the language of the contract is yet reasonably susceptible."); *Bd of Treasurers of the Internal Improvement Trust Fund v Lost Tree Village Corp*, 805 So 2d 22 (Fla 4th Dist App 2001) ("Where there is a latent ambiguity in a deed or contract, parol and other extrinsic evidence may be introduced to show the true intent of the parties."); *Kessler v Tortoise Development, Inc*, 134 Idaho 164, 1 P3d 292 (Idaho 2000) ("Extrinsic evidence may be used to show a latent ambiguity."); *Adams v Reinaker*, 808 NE 2d 192, 197 (Ind App 2004) ("That [latent] ambiguity cannot be resolved without extrinsic evidence to determine the intent of the parties to the agreement."); *In re Marriage of Holloway*, 999 P2d 980, 299 Mont 291 (Mont 2000) (District Court properly admitted parol evidence to explain a latent ambiguity in property settlement agreement.); *Alchemy Communications Corp v Preston Dev Co*, 558 SE 2d 231, 234; 148 NC App 219, 224 (NC App 2002) ("If a latent ambiguity exists, preliminary negotiations and surrounding circumstances may be used to determine what the parties intended."); *Dorsey v Contemporary Obstetrics & Gynecology*, 680 NE 2d 240, 13 Ohio App 3d 75, 84 (Ohio App 2d Dist 1996) ("Where a latent ambiguity exists, extrinsic

(d) There Is No Reason To Exclude Extrinsic Evidence In Order To Determine What The Parties Meant By The Language They Used.

How are the parties or the court hurt by an inquiry outside of the contract to determine if a disputed term may have more than one meaning? If the parties did enter into an agreement where both parties intended that white should mean black, shouldn't the court enforce that agreement? In terms of the Pool's constitutional argument, are not the courts *required* to enforce that agreement when freely made between the parties? To rule that "white means white" in such a case would be very much the case of the court making an agreement different from the parties. Further, if the Pool has its way, the court could not even consider the testimony of one or even a dozen disinterested individuals that the defendant party had told them "Yes, white does mean black," because that would be testimony beyond the four corners of the contract.

Certainly, the court's judicial resources are scarce and there is an incentive after a dispute has arisen for a party to attempt to manufacture an ambiguity in the hopes of bamboozling the court. Corbin recognized there are limits on circumstances where a court will give consideration to a claim that "white" means "black" or the like:

> "The more bizarre and unusual an asserted interpretation is, the more convincing must be the testimony that supports it. Just when the court should quit listening to testimony that white is black and that a dollar is fifty cents is a matter for sound judicial discretion and common sense. Even these things may be true for some purposes." 3 Corbin on Contracts (1960), § 579, p 420.

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evidence may be offered to determine the intended meaning of the parties."); *Z & L Lumber v Nordquist*, 502 A2d 697, 348 Pa Super 580, 587 (Pa Super 1985) (Extrinsic evidence of parties interpretation of contract found to contain latent ambiguity was given great weight where it consisted of the parties' conduct after contract formation.); *Hamblen County v City of Morristown*, 656 SW2d 331, 334 (1983); *Galloway Corp v SB Ballard Constr Co*, 464 SE 2d 349, 355; 250 Va 593, 502 (Va 1995) (Court found the use of parol and other extrinsic evidence was admissible to determine the intention of the parties where there existed a latent ambiguity.).

This is a task traditionally within the province of judges and routinely performed with regard to many other factual matters as discussed in subsection F below.

(e) This Case Does Not Involve The Constitutional Right To Contract, But The Every Day Obligation Of A Court To Determine The Nature Of A Contract Which The Parties Have Made.

The loser in every dispute over the meaning of contract leaves the court arguing the court has forced on it a contract it did not make. That argument has merit, however, when the court has failed to fully consider just what that party's contract was.

The "four corners" rule advocated by the Pool clearly defeats the parties' rights to have their contract enforced, because it substitutes a judge's understanding for that of the parties, as Corbin clearly explains. Corbin, *The Interpretation of Words and the Parol Evidence Rule*, 50 Cornell Law Quarterly 161, 162, 164 (1965):

> "The cardinal rule with which all interpretation begins is that its purpose is to ascertain the intention of the parties. The [four corners rule], as actually applied excludes proof of their actual intention. It is universally agreed that it is the first duty of the court to put itself in the position of the parties at the time the contact was made; it is wholly impossible to do this without being informed by extrinsic evidence of the circumstances surrounding the making of the contract. .... ftn 2"
>
> "ftn 2. Unless the court wishes to make the contact for the parties in the sole light of its own linguistic education and experience, it must always know the situation and relation of the parties and its dominant purpose. Without thus putting itself in the position of the parties, a court cannot know whether the language of the contract is susceptible of more than one interpretation, cannot determine the dominant purpose of the parties, and cannot arrive at the reasonable and sensible meaning."
>
> "[W]hen a judge refuses to consider relevant extrinsic evidence on the ground that the meaning of written words is to him plain and clear, his decision is formed by and wholly based upon the completely extrinsic evidence of his own personal education and experience.... [Where the judge relies solely on his background] he should realize that this evidence, known only to himself, may not be the best evidence; that he must hold it at every point subject to correction; and that the purpose of all the evidence is the ascertainment of the intention of the parties (*their* meaning), and not the meaning that the written words convey to himself or to any third persons, few or many, reasonably intelligent or otherwise."

Thus the four corners rule "results at times in the court's making a contract for the parties in disregard of their actual intention." *Id*, p 161.

Recently in *Klapp v United Ins Group Agency, Inc*, 468 Mich 459, 476; 663 NW2d 447 (2003), this Court disapproved use of the rule of *contra proferentem* in favor of consideration of extrinsic evidence because:

> "Such evidence [extrinsic evidenced of the defendant's prior course of dealing] at least affords a way by which to ascertain the parties' intent, unlike the rule of *contra proferentem*, which focuses solely on the status of the parties to a contract. ftn 15.
>
> "ftn15 Regardless of whether a contract is drafted with or without bilateral negotiations, looking at relevant extrinsic evidence to help determine the parties' intent where their contractual language is ambiguous better comports with the ultimate goal of 'honoring the intent of the parties,'... than does the rule of *contra proferentem*."

The "four corners" ruled urged by the Pool has the same failing when the question is whether the obvious reading of contract language actually captures the parties' intent.

(f) Although Contract Interpretation Is A "Matter Of Law," The Process Inherently Requires The Court To Resolve Questions Of Fact.

The Pool argues that in the first instance, the question of ambiguity is a question of law for the court. The Pool appears to argue that because the preliminary question of whether contract language is ambiguous is a "question of law," fact finding by the court has no part in the exercise. That view misunderstands the court's role. As explained by Professor Thayer long ago, Thayer, *Preliminary Treatise On Evidence At the Common Law* (Boston, Little, Brown and Company) (1898), pp 185, 203-04:

> "Courts pass upon a vast number of questions of fact that do not get on the record, or form any part of the issue. Courts existed before juries; juries came in to perform only their own special office; and the courts have always continued to retain a multitude of functions which they exercised before ever juries were heard of, in ascertaining whether disputed things be true."

> "Among questions of fact which are commonly treated in this way a conspicuous illustration is found in the construction of writings. It is not uncommon to call the interpretation and construction of writings "a pure question of law." That it is a question for the judge there is no doubt. But when we consider to what an extent the process of interpretation is that of ascertaining the intention of the writer, -- his expressed intention, -- irrespective of any rules of law whatever, and when we come to undertake the details of such an inquiry, it is obvious that most of this matter is not referable to law but to fact. The judge has to ascertain the usual meaning of words in the vernacular language, and what modifications of that meaning are allowable as a mere matter of the fair use of language; also, the fair meaning or the permissible meaning of the composition of these words....Moreover 'the meaning of words varies according to the circumstances of and concerning which they are used.' When once these circumstances are known, *i.e.*, all the extrinsic facts which may legally affect the interpretation, then the courts exercise the right to determine the bearing of these facts on the words of the writing, and the combined effect of words and facts as touching the expression of intention. This may not involve any question of law in the exact sense, for the answer may depend on no legal rule, but only on the rules, principles, or usages of language and grammar, as applied by sense and experience. So far, then, as the meaning of a document is to be determined merely by reading it in the light of ascertained facts, attending the making of it, we are presented with no question of law, in any strict sense of the word; it is a question for the court, but not a question of law."

See likewise, 3 Corbin on Contracts (1960), § 595.

This fact finding role clearly operates in our evidentiary system today. The Michigan Rules of Evidence require that certain preliminary factual questions be answered by a judge before being passed to a jury. MRE 104. These questions include questions regarding the admissibility of evidence and the relevancy of evidence when conditioned upon the fulfillment of some other fact. MRE 104(a) and (b). The Rules of Evidence do not apply to "[t]he determination of questions of fact preliminary to admissibility of evidence when the issue is to be determined by the court under Rule 104(a)." MRE 1101(b)(1).

(g) The Parol Evidence Rule Does Not Pertain Here.

The Parol Evidence Rule does not apply when evidence is offered to explain the contract's terms, *Romska v Opper*, 234 Mich App 512; 594 NW2d 853 (1999), 2 Restatement Contracts, 2d, §213, Comments a and b, or to show that a term is ambiguous. *Mid-American*

Management v Dept of Treasury, 153 Mich App 446; 395 NW2d 702 (1986). As noted at the outset, the Park and the Pool agree that their contract includes a pollution exclusion clause and that that clause contains an express definition of pollution.

Evidence of the course of dealings between the Park and the Pool under the succession of similar or identical insurance contracts is not within the Parol Evidence Rule because i) it concerns dealings between the parties *after* contract formation and ii) it does not "contradict, vary, or modify" the agreement between the parties because the policy does not expressly state, one way or the other, whether sewage is pollution. Therefore, the Pool's reliance on *Zilwaukee*'s prohibition of the use of parol evidence is misplaced and does not apply.

The Pool also relies on a footnote in *Upjohn Co v New Hampshire Insurance Co*, 438 Mich 197, 205, n 6; 476 NW2d 392 (1991), for the proposition that extrinsic evidence should not be allowed to ascertain the meaning of the pollution exclusion clause if the clause is found to be unambiguous. In *Upjohn*, the court rejected the dissent's opinion that the drafting history of the pollution exclusion clause should be taken into account in that case when examining whether the clause was ambiguous. *Id.* In our case, Court of Appeals' holding did not purport to allow evidence of prior negotiations (like drafting history) between the Grosse Pointe Park and the Pool to clarify the contract, nor does Grosse Pointe Park seek to introduce drafting history.

(h) There Are Ample Grounds In This Case For The Court To Determine That The Meaning Of Pollution Vis A Vis Sewage In The Pool's Contract Is Ambiguous.

When presented with uncontradicted evidence that the Pool covered thousands of sewage claims in the 1990s without ever asserting sewage was "pollution" within the meaning under the contract, the Court of Appeals correctly found that the term pollution was ambiguous. Put another way, on these facts it would not be unreasonable for a trier of fact to conclude that the insurance contract covered sewage claims, notwithstanding that the pollution exclusion clause

would appear at first blush to bar such coverage. The Pool's public statements that it covered sewage backups until April, 2000 corroborate the Court of Appeals' determination on that point. Accordingly, this Court should find the term "pollution" to be ambiguous and move to the second stage of applying the extrinsic evidence to determine whether the term pollution in the contract encompasses sewage. For the reasons set forth in the next section of this brief, when it performs that evaluation, this Court should find no question of material fact on this issue and enter judgment as a matter of law for the Park.

III

UNCONTRADICTED EXTRINSIC EVIDENCE SHOWING THE POOL'S CONSISTENT PRACTICE OF COVERING THOUSANDS OF SEWAGE CLAIMS DEMONSTRATES, THAT THERE IS AN AMBIGUITY IN THE MEANING OF POLLUTION UNDER THE INSURANCE CONTRACT, AND THAT THERE IS NO QUESTION OF MATERIAL FACT THAT THE CORRECT MEANING OF POLLUTION UNDER THE POLICY DOES NOT INCLUDE SEWAGE.

Here extrinsic evidence amply supports the conclusion that although sewage is often considered to be pollution, the Pool and the Park did not consider the pollution exclusion clause to encompass sewage. The evidence is based on both the Pool's consistent course of performance under the contract and its public admissions that it covered sewage claims until April 2000. Courts find evidence of course of performance to be highly probative of a party's interpretation of a contract.

(a) An Insurance Policy, Where Ambiguous or Susceptible to Several Meanings, Must Be Construed in Favor of the Insured.

Courts must examine the language of insurance policies and interpret their terms in accordance with well-established Michigan principles of construction. *Arco Indus Co v Am*

Motorists Ins Co, 448 Mich 395, 402; 531 NW2d 168 (1995),[7] *Michigan Millers Mutual Ins Co v Bronson Plating Co*, 197 Mich App 482; 496 NW2d 373 (1992); *aff'd* 445 Mich 558, 567; 519 NW2d 864 (1994). In interpreting ambiguous terms of an insurance policy, courts will construe the policy in favor of the insured. *Auto Club Ins Ass'n v DeLaGarza*, 433 Mich 208, 214; 444 NW2d 803 (1989). In an insurance policy, an ambiguity is broadly defined to include contract provisions capable of conflicting interpretations. *Id* at 208. In *Raska v Farm Bureau Ins Co*, 412 Mich 355, 362; 314 NW2d 440 (1982), the court held that:

> "If a fair reading of the entire contract of insurance leads one to understand that there is coverage under particular circumstances and another fair reading of it leads one to understand there is no coverage under the same circumstances the contract is ambiguous and should be construed against its drafter and in favor of coverage."

That principle is applied as a "tie-breaker" in favor of the nondrafting party after consideration of extrinsic evidence and other rules of interpretation have failed. *Klapp, supra*

The insurer also has the burden of proof as to exclusions. *Michigan Mutual Liability Co v Ferguson*, 15 Mich App 298; 166 NW2d 525 (1968).

(b) The Court Of Appeals Properly Considered The Parties' Course Of Dealing As A Means By Which To Interpret The Insurance Contract. [8]

The parties' dealings under the contract and under similar contracts are a proper means by which to interpret a contract.

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[7] Note that *Arco* has been partially overruled on points of insurance law not applicable to issues in this case by *Frankenmuth Mut Ins Co v Masters*, 460 Mich 105, 595 NW2d 832 (1999).

[8] The Pool asserts in its Statement of Facts, Pool S Ct Brief at 14, that the Park did not challenge in the trial court the Pool's assertion that sewage was pollution. That is incorrect. In its Brief In Support of its Motion for Partial Summary Judgment as to Inapplicability of the Pollution Exclusion, at p 8, App. 37b, the Park argued, as it did in the Court of Appeals and does here, that course of dealing evidence "suggests, if not proves, that the Pool, as determined by its previous course of conduct, does not considered CSF [combined sewage flow] to be a 'pollutant' as that term is defined by the Policy...."

> "Even without explicit incorporation, an agreement may be fleshed out by usages to which the parties are subject, by a course of dealing between the parties prior to their agreement, or by a course of performance between them after their agreement." *Dumas v Auto Club Ins Ass'n*, 437 Mich 521, 602, n 59; 473 NW2d 652 (1991), citing with approval, Farnsworth, Contracts, §3. 28, p 196.

Course of dealing is a contract interpretation doctrine defined by the 2 Restatement Contracts, 2d, §223, pp 157-158, (cited with approval by *Dumas*) as:

> "(1) ... a sequence of previous conduct between the parties to an agreement which is fairly to be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct.
>
> (2) Unless otherwise agreed, a course of dealing between the parties gives meaning to or supplements or qualifies their agreement."

Course of performance is a similar doctrine which looks to how the parties actually performed the contract at issue. 2 Restatement Contracts, 2d, § 202, comment g, pp 90-91, provides that:

> "Where an agreement involves repeated occasions for performance by either party with knowledge of the nature of the performance and opportunity for objection to it by the other, any course of performance accepted or acquiesced in without objection is given great weight in the interpretation of the agreement."
>
> "The parties to an agreement know best what they meant, and their action under it is often the strongest evidence of their meaning. But such 'practical construction' is not conclusive of meaning. Conduct must be weighed in light of the terms of the agreement and their possible meanings."

See also, Detroit Greyhound Employees Federal Credit Union v Aetna Life Insurance Co, 381 Mich 683, 692; 167 NW2d 274 (1969)

> "[W]hatever is done by the parties during the period of the performance of the contract is done under its terms as they understood and intended it should be. Parties are far less likely to have been mistaken as to the meaning of their contract during the period when they are in harmony and practical construction reflects that meaning than when subsequent differences have impelled them to resort to law and one of them then seeks a construction at variance with their earlier practical construction of its provisions." quoting with approval, 17 Am Jur 2d, Contracts, § 274, p 685.

> "There is no requirement that an agreement be ambiguous before evidence of a course of dealing can be shown, nor is it required that the course of dealing be consistent with the meaning the agreement would have apart from the course of dealing." 2 Restatement Contracts, 2d § 223 comment b, p 158.

Course of dealing and course of performance evidence may be compelling. "Where parties by such a uniform course of conduct for a long time have given a contract a particular construction, that construction will be adopted by the courts." *Klapp*, 468 Mich. at 479 (relying on evidence of the defendant's practice of paying other employees commissions under circumstances similar to the plaintiff's to construe ambiguous language in favor of the plaintiff).

In fact, application of this doctrine is so well accepted it is part of the Uniform Commercial Code, codified in Michigan as MCL 440.1205, 2202 and 2208, and applies to the thousands of commercial contracts made in this state each year. "[T]he course of performance by the parties is considered the best indication of what they intended the writing to mean." MCL 440.2202, comment 2.

Michigan courts have considered evidence of how insurers have handled other similar claims with other insureds has been found to be relevant to interpret an insurance contract. In *Mich Millers Mut Ins Co v Bronson Plating Co*, 197 Mich App 482, 494 -95; 496 NW2d 373 (1992), *aff'd on other grounds,* 445 Mich. 558; 519 NW2d 864, (1994),[9] the court of appeals held that evidence of whether an insurer had provided coverage in response to PRP demand letters to other insureds was relevant to determining whether the insurer considered such letters to be "suits" under the insurance policy. *See also, Terry Barr Sales Agency, Inc v All-Lock Co, Inc*, 96 F3d 174 (6th Cir, 1996) (Under Michigan law, the parties' practical interpretation of their contract, and their course of conduct under that contract, are entitled to great weight in

interpreting ambiguous provisions of the contract.). See also, *Vormelker v Oleksinski*, 40 Mich App 618, 626; 199 NW2d 287 (1972), where the insurer's course of dealing with other insureds was considered in order to interpret contract terms:

> "When the evidence offered is of other contracts between the same parties, [courts] have been willing to acknowledge that other similar contracts showing a custom, habit or continuing course of dealing between the same parties may be received as evidence of the terms of the present bargain....Contracts of a party with third persons may show the party's customary practice and course of dealing and thus be highly probative as bearing on the terms of his present agreement."

Cf, Quality Products and Concepts Co v Nagel Precision, Inc, 469 Mich 362, 364-65; 666 NW2d 251 (2003), where, the Court ruled that parties to a written agreement could modify it or waive its conditions by mutual assent notwithstanding a "no modification" clause, and repeated at several points that such assent could be proven by a course of performance. While the plaintiff failed in that case because he could not show any course of performance by the defendant; here we can show numerous instances over a succession of identical contracts where the Pool covered sewage claims made by the Park. Likewise, the Pool's reservation of rights letter can be seen as a failed attempt to modify the coverage under the Policy, because the Park, like the defendant in *Quality Products*, never consented by word or action to that proposed modification and in fact objected to the letter after it was sent.

(c) Case Law Emphasizes The Importance Of Examining the Specific Policy and Relationship Between the Parties in Construing the Scope of the Pollution Exclusion Clause.

Although the Pool argues that the definition of pollution under its pollution exclusion clause unambiguously includes sewage, a review of case law across this country underscores the point that this inquiry is specific to the individual policy and to the relationship between the

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[9] The opinion in the Supreme Court did not address the court of appeals' ruling that evidence of the insurer's handling of other PRP letters was relevant to determining whether such letters were "suits" within the meaning of the policy.

specific insurer and insured. While the Pool cites a number of cases in which courts have held that the various definitions of pollution in the policies at issue were unambiguous, none involved facts like those here, where the contracting party is a self insurance pool writing coverage intended to address liability issues relevant to municipal operations and who paid on every one of thousands of sewage claims. Further, on its own website, the Pool concedes it covered sewage back up claims through April 2000. App. 685b – 686b.

There are a number of cases involving sewage where the courts have held on the facts of the case before them that the pollution exclusion coverage did not bar coverage for a variety of reasons. *See for example, Keggi v Northbrook Property and Cas Ins Co,* 199 Ariz 43; 13 P3d 785 (2000), *Meridian Mutual Ins Co v Kellman*, 197 F3d 1178, 1181 (6th Cir, 1999) ("Many courts, including the Sixth Circuit, have held that a pollution exclusion clause in a CGL insurance policy applies only to injuries caused by traditional environmental pollution."), *Incorp Village of Cedarhurst v Hanover Ins Co*, 89 NY2d 293; 675 NE2d 822; 653 NYS2d 68 (1996); *Minerva Enterprises, Inc v Bituminous Cas Corp*, 312 Ark 128; 851 SW2d 403 (1993); *USF&G v Armstrong*, 479 So2d 1164, 1168 (Ala, 1985); *Guenther v City of Onalaska*, 223 Wis 2d 206, 214; 588 NW2d 375 (1998); *Titan Holdings Syndicate, Inc v City of Keene, NH*, 898 F2d 265 (CA 1, 1990); *Smith v Reliance Ins Co of Illinois*, 807 So 2d 1010 (La App, 2002).

One of the opposing authorities cited by the Pool is worthy of brief discussion. The Michigan Court of Appeals in *MMRMA v Seaboard Surety Co,* C of Appeals No 235310 (August 7, 2003), 2003 WL 21854655 (Mich App)(Exhibit 2 to the Pool's S Ct brief), held sewage under the Seaboard Surety policy was pollution. MMRMA sued on a subrogation theory to recover its payment of a sewage back up claim asserted against Westland allegedly caused by Seaboard Surety's insured. MMRMA covered that claim although its policy had a pollution exclusion

clause; see App 693b-696b (MMRMA's Application for Leave to Appeal to the Supreme Court, S Ct. Docket No 124882.(filed October 27, 2003), p. 4 and Exhibit F), demonstrating that while one insurer may consider sewage to fall within its pollution exclusion clause, another may not. It is of some relevance here that the plaintiff "insurer," MMRMA, is a Michigan governmental self insurance pool which offers competing coverage to the Pool.

The point of this discussion is not that this Court should follow one line of authority or another but that the correct inquiry is the "applicable insurance policy" between the Park and the Pool, as the Court's November 5, 2004 Order specified.

(d) Because There Is No Dispute That the Pool Has Consistently Interpreted the Pollution Exclusion as Not Applying to Sewage, This Court Should Summarily Affirm The Trial Court's Judgment That The Pollution Exclusion Clause Does Not Bar Coverage.

On the facts of this case, there can be only one conclusion. There were a succession of identical insurance contracts before and after the 1994/1995 Policy under which the Pool paid and paid and paid again on sewage claims without ever claiming sewage was pollution. It paid the Park's sewage claims before the filing of the *Etheridge* suit, during the *Etheridge* suit, and after that suit was settled. It even paid three prior sewage claims under the 1994/1995 policy. It also paid every sewage claim its other municipal insureds tendered without claiming sewage was pollution. It has stated publicly that it offered sewage back up coverage through April, 2000. In the face of that history, it still argues that its policy does not cover sewage. Neither the trial court nor the Court of Appeals bought its argument nor should this Court.

The Pool cannot claim that the *Etheridge* claim fails because the *Etheridge* facts are somehow distinctly different from other sewer backups which it has covered without reservation. Like the Park residents in 1994 and the *Walters* plaintiffs in 1996, the *Etheridge* plaintiffs claimed their basements flooded from sewer backups, App. 416a, *Etheridge* Second Amended

Complaint, ¶ 43. The Pool readily admitted that the sewage is the exact same substance whether it ends up in a Grosse Pointe Park basement or in the basement of a house in Detroit. App. 232a, 234a-237a, 1/7/00 Hearing Transcript pp 27, 29-32. The Pool offered no factual support to explain why the *Etheridge* sewage was pollution when all other sewage was not.

This Court should hold that that there is no question of material fact and rule as a matter of law that sewage is not pollution under the policies issued by the Pool Thus this Court should affirm the judgment of the trial court on this point and reverse that part of the Court of Appeals' ruling which remanded this case to the trial court for fact findings on that issue.

IV

THE COURT OF APPEALS CORRECTLY HELD THE PARK COULD RAISE THE DEFENSE OF ESTOPPEL TO THE POLLUTION EXCLUSION CLAUSE BECAUSE THE PARK WAS JUSTIFIED IN ITS RELIANCE ON THE POOL'S COVERAGE OF OTHER SEWAGE CLAIMS.

(a) An Insurer Can Be Estopped To Deny Coverage When It Has Misrepresented Coverage And The Insured Has Acted In Reliance To Its Detriment.

The Pool admits, Pool S Ct Brief, p 40, there are two exceptions that allow the doctrine of waiver or estoppel to be applied to broaden coverage, one of which is "where the inequity of forcing the insurer to pay on a risk for which it never collected premiums is outweighed by the inequity suffered by the insured because of the insurance company's actions." *Lee v Evergreen Regency Co-Op & Mgt Systems*, 151 Mich App 281, 287; 390 NW2d 183 (1986). *See also, Kirschner v Process Design*, 459 Mich 587, 595; 592 NW2d 707 (1999), *Smit v State Farm Mut Ins Co,* 207 Mich App 674, 679; 525 NW2d 528 (1994). During argument in the circuit court, the Pool conceded that estoppel is justified when "a party intentionally or negligently induces another party to believe facts and the other party justifiably relies and acts on this belief and will

be prejudiced if the first party is permitted to deny the existence of the facts." App. 241a, January 7, 2000 Hearing Transcript, p 36.

One element of *Lee* can be quickly addressed. In balancing the equities under the *Lee* case, no evidence in this case was adduced to show that the Pool did not set its premiums based on covering sewage back up claims. It admits it consistently covered claims for sewage backups on behalf of the Park and other members of the Pool for a number of years. Where the Pool was routinely covering backups, if it did not adjust its premiums accordingly, it has only itself to blame.

The Pool acknowledges *Lee* applies where the insurance company misrepresented the terms of the policy to be insured, quoting *Lee* at 287. Pool S Ct Brief, p 41. Contrary to the Pool's suggestion, the "misrepresentation" rule for estoppel does not include the limitation that only misrepresentations *before* a loss are actionable. The Pool's argument to that effect is based on brief *dictum* in *Smit v State Farm Ins Co*, 207 Mich App 674 (1994), which stated in passing that the misrepresentation in *Industro Motive Corp v Morris Agency, Inc,* 76 Mich App 390 (1997), occurred before the loss. This emphasis is both misleading and misplaced. While the misrepresentation in *Industor Motiv* did in fact occur before the loss in that case, the court in *Industor Motiveo* neither relied on nor even noted the timing of the misrepresentation in affirming the estoppel. The decisive fact in *Industro Motive*, as well as the other cases cited by the Pool, was that the insurance agent or the insurance company made a misrepresentation to the insured and the insured relied on this misrepresentation to their detriment. When the misrepresentation occurred was not relevant. Moreover, *Allstate Ins Co v Snarski*, 174 Mich App 148 (1998)(cited by the Pool), the misrepresentation as to the need to make a late premium payment to keep coverage in place occurred the day *after* the insured's accident This case

illustrates that the importance is not the timing of the misrepresentation in relation to the loss, merely that a misrepresentation caused detriment to the insured.

The Pool aptly points out that estoppel could be "based on misrepresentations *or actions* upon which the insured relied." Emphasis supplied Pool S Ct Brief, p 41. Actions do speak louder than words. By the time the *Etheridge* suit was filed, the Pool had covered a sewage claim under the 1992/1993 policy, 68 claims under the 1993/1994 policy, and three claims under the 1994/1995 policy. By the time the Pool denied coverage in *Etheridge* in late August, 1997, the Pool had also told the Park it would cover the sewage claims in the *Walters* class action suit without any reservation of rights, it had told the Park it would recommend covering the settlement for least at $750,000, and it had participated in settlement discussions as if it had a stake in the outcome.

Although there are no Michigan estoppel cases involving an insurer's failure to notify its insured of its decision to deny coverage until the insured had acted to its prejudice, the Florida Supreme Court has also held that an insurer must make a prompt determination of coverage decisions or be estopped from denying coverage. *Tiedtke v Fidelity & Casualty Co*, 222 So 2d 206 (Fla 1969). The insurer provided a defense for the insured's lawsuit for almost a year and a half under the reservation that it could disclaim liability at a later date Then immediately after an adverse judgment was returned against the insured, the insurer specifically denied coverage and refused to satisfy the judgment. The court concluded that the insurer obviously breached its obligation to its insured "to inform him of the fact of its disclaimer of liability within a reasonable time." *Id* at 209. The court state the rule as:

> "If an insurer intends to stand on any forfeiture reservation, it should inform the insured as soon as practicable after it has ascertained facts upon which it bases its forfeiture. In the instant case, it is apparent that many months before the trial, the Company had gathered all the information it needed for either the defense of the

> suit or for raising the forfeiture issue and disclaiming liability. Each case of this nature must, of course, be considered on its own merits." *Id* at pp 209-210.

In making its decision, the court cautioned insurers it had previously stated that "nonwaiver agreements [like a reservation of rights letter] are valid, but coupled this with a cautionary statement that such agreements do not have the unfettered power in all circumstances to supercede the doctrines of waiver and estoppel." *Id.*

As the Pool notes, if an insurer is found to have unreasonably delayed in issuing a reservation of rights letter, it will be estopped from asserting its policy defenses. The cases are decided on a fact specific basis often hinging on the degree of prejudice to the insured from delayed conveyance of the notice. *Multi-States Transport, Inc v Michigan Mutual Inc*, 154 Mich App 549; 398 NW2d 462 (1986), *lv den* 428 Mich 866 (1987)(an insured who waited until the eve of trial, 2.5 years after the filing of the complaint, to provide its insured with a reservation of rights letter was estopped from asserting policy defenses); *Allstate Ins v Keillor*, 203 Mich App 36; 511 NW2d 702 (1993), *affd* 450 Mich 412, 537 NW2d 589 (1995) (a five month delay in issuing a reservation of rights letter was an acceptable amount of time to provide insured with notice of possible denial of coverage); *Fire Ins Exchange v Fox*, 167 Mich App 710; 423 NW2d 325 (1988) (four months was an acceptable delay in issuing a reservation of rights letter); *Cozzens v Bazzani Bldg Co*, 456 F Supp 192 (ED Mich 1978) (notice of reservation of rights was sent to insured two years after filing complaint and two weeks before trial, court held insurer estopped from asserting policy defenses.)

Michigan courts have found estoppel an appropriate remedy because the availability or lack of insurance has a significant bearing on how an insured conducts its defense and negotiates settlement. This Court explained that when there is a potential conflict between the insurer and

its insured over the scope of coverage, the insurer has a special duty that the insurer act promptly and forthrightly with its insured. *Meirthew v Last*, 376 Mich 33; 135 NW2d 353 (1965).

> "When a conflict of interest [over coverage]–even a mere possibility thereof–arises, the law suggests (if it does not require) that the insurer act promptly and openly, on peril of estoppel, preferably upon a record made in the pending case (if pending as here) with the court fully apprised of all necessary details; also that the insurer act thus on time for arms' length actions which may protect the respective rights of both parties to the contract of insurance." *Id* at 355

The *Meirthew* Court estopped the insurer from raising the policy defense because it found the insurer's original notice "legally insufficient" under a "reasonableness test" comprised of two elements: timing and content: "[I]t was unreasonably and prejudicially tardy. It failed that test because it left Last in the dark as to the nature of the policy defense or defenses the insurer had in mind." *Id* at 356.

Likewise, the court in *Cozzens v Bazzani Building Co*, 456 F Supp 192 (ED Mich 1978), found presumptive prejudice results from a finding of untimely notice. A complaint was filed against the insured on July 31, 1975. A verbal reservation of rights was conveyed to the insured in June, 1977. The case was set for trial on April 4, 1978. So, the insurer waited until two years after the complaint was filed and ten months before trial to inform the insured of its intention to deny coverage. The court found:

> "[T]he carrier owes certain responsibilities not only to the insured but also to the opposing party and to the court. It is a well-known fact that the availability of an insurance fund to pay whatever judgment is ultimately entered is an important element in the management of a case, both with respect to the nature and extent of the discovery that is undertaken and with respect to the course of settlement discussions. As for the Court, it bears the responsibility of administering our system of justice in an orderly and expeditious manner. Those interests are not served where, as here, a conflict between the two parties to the contract of insurance is not brought to light until the very day of trial. In light of the many diverse interests involved, this Court joins its voice with that of the Michigan Supreme Court in urging that the insurer act promptly and openly, on peril of estoppel, preferably upon a record made in the pending case (if pending as here) with the court fully apprised of all necessary details; . . ." *Id* at 202.

Here the Pool waited until just one month before trial and one day after a tentative settlement was reached to belatedly inform the Park of its coverage decision made three weeks before.

The considerations which justify estoppel where reservation of rights letters are provided untimely are even more compelling whether a coverage denial is involved.

Taking the lead from Judge O'Connell's partial dissent in the case below, App. 44a, Dissent's Slip Op p 2, the Pool cites to several Michigan cases and cases from other states for the proposition that payment of other claims under a policy does not waive or estop an insurer's right to deny a later claim. Pool S Ct Brief at 49-50. As is emphasized by the Pool's parenthetical description of each case, all of the cases cited involved the insurer's payment of just *one* claim, not the payment of many different claims. In this case, the Pool paid three other sewage claims arising under the same 1994/1995 policy and during the pendency of the *Etheridge* suit stated it would cover a subsequent sewage back up class action suit under an identical policy. Further, none of those cases were coupled with a factual scenario where the insurer decided to deny coverage but waited until after its insured had committed to a multimillion dollar settlement to tell its insured. Thus those cases do not apply to the facts at hand.

(b) The Park Has Provided Sufficient Evidence Of Misrepresentations, Reliance And Detriment To Proceed To Trial.

The Pool's second argument on this issue is that the Park has failed to make even a minimal factual showing on the elements of its estoppel claim and it should be granted summary disposition under MCR 2.116(C)(10). When considering a (C)(10) motion, all evidence must be reviewed in the light most favorable to the non-moving party, *Hazle, supra,* and all reasonable factual inferences must be drawn in favor of the non-moving party – in this case the Park's favor. Proof of reliance and detriment are by their very nature questions of fact to be determined by the jury. See *Westfield Cos v Grand Valley Health Plan*, 224 Mich App 385, 390; 568 NW2d 856

(1997), *Pursell v Wolverine-Pentronix, Inc*, 91 Mich App 700, 704; 283 NW2d 835 (1979). The trial judge also had presided over the *Etheridge* case and was therefore intimately familiar with its development. The Park, in its summary disposition motions, specifically requested that she take judicial notice of all that had transpired in the *Etheridge* litigation. App. 65a, Plaintiff's Common Statement of Facts, p 2. Judge Hathaway held that the Park had so convincingly proved estoppel that she granted judgment in the Park's favor on this point. "Factual findings of trial judges in such matters are entitled to great weight on appeal." *People v Richardson*, 469 Mich 916, 928; 669 NW2d 797 (2003).

The Pool took the following acts which could be and were interpreted to mean that the Pool would not deny coverage under the pollution exclusion clause. First, there was the consistent repeated covering of sewage claims before and during the suit. Second, the Pool's reservation of rights letter did not deny coverage or represent but only advised that some part of the damages might not be covered. "We are reserving our rights to restrict payment to those owed under the contract coverage." App. 447a – 449a. The Pool's agreement in 1996 to cover the *Walters* suit without a reservation directly contradicted the Pool's *Etheridge* reservation letter from 1995, suggesting the Pool had changed its position. The Pool remained closely involved in the *Etheridge* case. At a meeting between the Pool, the Park and defense counsel on July 24, 1997, three weeks before attending the first court-ordered settlement facilitation ordered by Judge Hathaway, the Pool's representatives stated they would recommend settlement authority in the amount of $750,000, a recommendation consistent with coverage and inconsistent with a denial of coverage. The Pool has never explained why Ms. Garrison, although she knew coverage had been denied and had been instructed on or about August 4 to tell the Park, failed to do so, notwithstanding repeated opportunities.. Instead she dropped just one veiled hint about

"potential coverage issues." Even though the Pool had denied coverage, Ms. Garrison attended and participated in the settlement discussion on its behalf, and never told the Park, its attorney, the facilitator or opposing counsel that there was no coverage--although all would agree that the existence of insurance coverage is a material consideration in settlement. What was she doing at the settlement conferences unless the Pool had something at stake?

It is undisputed that representatives of the Park relied on the actions of the Pool to believe that coverage was afforded for the Etheridge claim. App 469a (Krajniak dep, p 170). After an initial discussion, Pool representatives never again mentioned the reservation of rights letter to the Park City Attorney, App 556a (Deason dep, p 119). Instead, Pool representatives discussed obtaining settlement authority (as much as $750,000) from the Pool. App 556a (Deason dep, p 120). This and other conduct let Deason to believe the Pool "was not relying on its reservation of rights letter." App 556a (Deason dep, p 121). In assisting Mr. McSorley in defending the case, the Park's City Attorney attended only to "affirmative relief issues" (*i.e.*, injunctive relief) but not the Etheridge plaintiffs' claims for monetary relief. App 553a-554a (Deason dep, pp 112-13).

The Pool argues that its failure to tell the Park it had denied coverage made no difference because the Park went through with the tentative settlement. The Court can well believe that if the Park had known the Pool had denied coverage, the Park would have negotiated hard to reduce the plaintiffs' demands while simultaneously bargaining Detroit's share of the settlement up from 50%. Would it have made a difference? We will never know for sure because the Park was effectively denied that opportunity, but at a trial of this matter evidence will be developed with regard to the effect of availability of insurance on settlement and the question whether the City of Detroit's settlement authority was greater than the $1,900,000 it offered will be explored.

But once a tentative settlement was reached, the dynamics of the situation tilted significantly against the Park. Where a party has agreed to settle at one amount, it has lost a great deal of leverage in subsequent negotiations. Further, the trial date was just weeks away. It must be remembered that the tort liability landscape has changed significantly since September, 1995. The *Etheridge* suit was filed on September 14, 1995, just before the 1995 tort reform legislation abolishing joint liability came into effect, 1995 PA 161 (eff September 26, 1995) and 1996 PA 249 (eff March 28, 1996). Accordingly, under the law which applied at the time suit was filed, if Detroit proceeded with the settlement but the Park did not, the Park would not be able to argue allocation of fault at trial as it could do under current law. Who would advise the Park to try a basement flooding case to a Wayne County jury without insurance coverage! Thus, Mayor Heenan well understood the Park's difficult situation when he testified, "[T]he risk is too great to consider going to trial and possibly having to pay $7,000,000" and that Detroit's one-half share of the settlement was "particularly favorable to the City of Grosse Pointe Park at that time." App. 552a-553a (Heenan dep, 87-88).

In the end, whether the Park's beliefs and reliance were at a level sufficient to justify invocation of the court's equity powers is best left to the trier of fact. There is certainly evidence in this record to support an inference favorable to the Park on these issues, justifying affirmance of the denial of the Pool's motion for summary disposition on this issue.

SUMMARY

After seven years of litigation over coverage, the Pool has yet to explain why it will not cover this claim and why it failed to tell the Park it was denying coverage as soon as that decision was made. It is clear the Pool covers sewage back up claims; it has never denied a single one but has never explained what makes the sewage in this case different. Likewise, the

Pool has testified that as soon as it made the decision to deny coverage, it told its employee to tell the Park, but Ms Garrison never did.

Perhaps Judge Hathaway deduced the real reason.

> "THE COURT:..They [the Pool] pay and they pay and they pay. Practice and procedure was to pay. Little claims, hundred and fifty, two hundred after the deductible, whatever it was for Grosse Pointe Park, but they paid these backups. *Probably because they believed under the policy they had to. That's my interpretation of the way the deposition of Garrison went*, under what she believed initially might have reserves of $50,000 so they pay. But now we're at 1.9 million, we're not going to pay. Why? Why pick and choose? Why not follow the policies? Why not follow the procedure?" App. 212a, January 7, 2000 Hearing Transcript, p 7.

Regardless of the Pool's motivation in arguing for a radical change in Michigan contract law, it has failed to present this Court with a sound policy reason to abandon this Court's rule that in performing its obligation to enforce the contract the parties have made, a court will not turn a blind eye to relevant, admissible and probative evidence of what that agreement is. As particular to this case, a court will consider relevant evidence to make a preliminary determination whether there is a question of fact whether language in a contract is susceptible to more than one meaning. It will do so even if, in the court's judgment, the language on its face appears clear and unambiguous, because the court recognizes its obligation is to determine what the language meant to the parties and not to the court.

The Court of Appeals has already held that the Park is entitled to coverage under Coverage A of the Policy pending only a determination of the application of the pollution exclusion clause. That holding is not subject to this appeal. This Court should affirm the Court of Appeal's order admitting extrinsic evidence of the meaning of the pollution exclusion clause and, because the evidence in favor of the Park's interpretation is uncontradicted, enter judgment in favor Grosse Pointe Park as a matter of law.

With regard to the Park's estoppel claim, the Pool admits it made a coverage decision but failed to communicate that decision to the Park in a clear, express and unequivocal way at a crucial point in the case. Michigan case law recognizes the critical importance insurance plays in litigation and permits estoppel when an insurer's actions have caused its insured to misunderstand its coverage to its detriment. The Park has made a sufficient showing to obtain a trial on its estoppel claim. Accordingly, this court should affirm the Court of Appeals on this issue.

Respectfully submitted,

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